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SUBJECT: SAUDI 2009 BUDGET APPROVED, BENEFITING FROM STRONG 2008 REVENUES

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¶1. (SBU) Summary: Amidst plunging oil prices and a struggling world economy, the Saudi cabinet endorsed a strong countercyclical 2009 budget on December 22, which local market analysts have widely praised. The new SAR 475 billion ($127b) budget is 6.9 percent less than actual 2008 expenditures of SAR 510b ($136b); however, actual expenditures here typically exceed budgeted levels, so 2009 expenditures likely will surpass 2008 levels. Following fiscal performance in 2008 that was the strongest ever recorded in this country's history, the SAG has budgeted a relatively small fiscal deficit of SAR 65b ($17.3b) in 2009, a figure dwarfed by the country's cash reserves and overseas investments. After several years of prudent budget management and incredibly high oil revenues, the new budget puts Saudi Arabia in a strong position to continue pursuing the SAG's development goals. End summary.

An expansionary budget for
challenging times

¶2. (U) On December 22, the Saudi Council of Ministers announced the results of fiscal year 2008 (the Saudi fiscal year is the calendar year) and endorsed the SAG's 2009 budget. The budget for fiscal year 2009 is the largest budget in the history of Saudi Arabia. It is a confidence building, expansionary budget. A variety of local economist contacts told econoffs that they believed the government is sending a strong confidence building message that in hard times the government will step in to support the economy. Increasing capital and current spending will support development programs and investments, which have an immediate effect on the private sector. Such an aggressive budget in the face of a bleak global economic outlook for 2009 is, according to local economists, intended to provide fiscal stimulus and revive the private sector.

¶3. (SBU) Local economists expect economic performance to deteriorate in 2009 as the Kingdom is affected by recession in most of the world's leading economies. For example, the influential Saudi firm Jadwa Investment forecast that Saudi economic growth will fall to 1.5 percent in 2009 from an estimated 5.7 percent this year (Note: In a December 21 meeting, Deputy Finance Minister Al-Baz'y told Econcouns that although the SAG estimated 2009 Saudi GDP growth would be lower than the 2008 level, he did not indicate that it would anywhere near that low). Oil prices are expected to be significantly lower this year and oil revenues will be exacerbated by production cuts. Analysts expect years of fiscal restraint, surpluses, foreign asset accumulation, and government debt reduction to help offset the expected depression in oil revenues. One local banking contact told econoff December 29 that although Saudi Arabia will continue to feel minor but painful stings as the effects of the global

financial crisis work their way through economic systems in unpredictable and perhaps unexpected ways, the new budget is further evidence that Saudi Arabia is "probably at least as well placed as any other country to weather this storm."

2008 budget performance

¶4. (U) The 2008 budget recorded a surplus of $157.3b, the largest ever in the history of Saudi Arabia, with spending at $136b and revenues of $293b. Nominal GDP grew by 22 percent, up from 9.4 percent in 2008. Real GDP growth in 2008 was 4.2 percent, up from 3.4 percent from last year. Per capita GDP rose to $18.5 thousand, the highest since 1981 when the country's population was 9.8 million compared to 25 million at present. 2008 witnessed the strongest fiscal performance ever recorded in the history of Saudi Arabia. Spending exceeded its budgeted total by 24 percent. Oil export revenues hit a historic high of $301 billion in 2008.

¶5. (U) The majority of the budget surplus was used to increase the stock of foreign assets at the Saudi Arabian Monetary Agency (SAMA). SAMA's net foreign assets rose by $144b. These assets currently stand at $444b. Local economists estimate that these reserves will earn around $20b in income this year. Government debt was also cut by $8b to $63.2b (13.5 percent of GDP).

¶6. (U) In 2008, non-oil private sector grew by 4.3 percent, the slowest rate since 2003. Transport and communication grew by 9.5 percent. Transport and telecoms expanded by 11.4 percent, due largely to mobile phone services. Electricity,

gas and water grew by 6.3 percent. Construction however expanded by a mere 4.1 percent due to contractor shortages and surge in raw material costs. The financial sector grew by only 2.2 percent. Inflation rose to an average of 9.2 percent, compared to 4.1 percent last year. The main sources of inflation were rents and the surge in global food prices this year.

2009 Budget forecast

¶7. (U) The SAG budgeted spending for fiscal year 2009 at $126b and revenues at $109.3b with a projected deficit of $17b. The new budget prioritizes developing schools, universities, clinics, waterworks, roads and telecommunications. New projects will include vocational schools, a women's university, primary care clinics, hospitals, sports clubs, roads and bridges, as well as improvements to ports and railway infrastructure. In addition $20 billion are to be made available to the real estate and finance industries. Spending was allocated as follows:

-- Education and manpower development is projected to rise to $32.5b, up $4.5b from the budgeted allocation for 2008, to open new schools, a female university and continue construction of educational institutions;

-- Health and social affairs, $13.8b, up $2.1b compared to the 2008 allocation;

-- Water and agriculture and infrastructure have been allocated $9.3b, up $1.8b from 2008. Funds have been budgeted for new projects and enhancement of sewage systems, wells and dams;

-- Transportation and telecommunications, $5b. This will cover 5,400 kilometers of roads to be added to the 30,000 kilometers currently under construction; and

-- Defense and security are believed to be the largest component of government spending accounting for one third of

the budget. These figures reportedly will be published in the coming months.

New budget based on Saudi oil
at approximately $36/barrel

¶8. (U) Oil sales accounted for 90 percent of government revenue in 2008, so the price trend over 2009 is the single most important factor in projecting the SAG's ability to achieve its capital investment objectives. The 2009 budget is based on an average Saudi oil price of around $36 per barrel (equivalent to about $43/barrel for West Texas Intermediate crude). In recent years, oil prices have greatly exceeded Saudi budgeted levels (resulting for example in 2008 revenues exceeding budgeted levels by 144 percent). However, that will not be the case as long as energy prices remain at, near, or below current levels. Regardless, much of Saudi Arabia's massive oil reserves may be the world's cheapest to produce, so even with very low prices, the country will continue to generate a large majority of total government revenues from the petroleum sector.

Comment

¶9. (SBU) The SAG's prudent budget management in recent years is expected to pay off now. It is worth underlining that during previous oil booms, Saudi ministers were graded mainly on how fast they could shovel money out the door, and huge sums were spilled on inadvisable megaprojects and extravagant personal spending by princes and their cronies. However, under the fiscally conservative leadership of King Abdallah and a finance ministry that kept its eye on the ball during several turbulent years, all that has changed. Our contacts in all the most powerful SAG ministries express awe and perhaps even a little intimidation over the careful oversight by, and tight purse strings of, Saudi finance ministry technocrats. During seven fat years of the most recent oil boom, Saudis griped that their government was not spreading the wealth fast enough. Now the Saudi people have cause to be grateful for their government's able stewardship.

¶10. (SBU) While economic growth is likely to slow down, driven by the current global recession, Saudi Arabia is well able to keep its head above water. The projected budget

deficit can be easily financed by tapping into the country's foreign asset reserves, and it may be replaced by a surplus if oil prices and production levels increase. However, non-oil private sector growth has fallen short of expectations, symptomatic of previous oil boom cycles. However, Saudi Arabia is in a much better fiscal position now than it was in the late 90s and therefore better able to boost its non-oil sector in spite of the global recession.
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